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Advancing Fairness in the Marketplace for All

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July 5, 2019

Senator Anna Caballero
State Capitol, Room 5052
Sacramento, CA 95814

Re: S.B. 472, Earned Income Access Service Providers Act (Oppose)

Dear Senator Caballero:

The National Consumer Law Center, on behalf of its low income clients, regretfully opposes the current version of S.B. 472, Earned Income Access Service Providers Act. While our previous position was support if amended, the amended version fails to address the critical issues we discussed in our April 24, 2019 letter**.** Indeed, in many respects, the amended bill is even worse than the original bill. While we appreciate the intent of helping providers to develop better alternatives to payday loans, as well as concerns about securing regulation for products already on the market, we feel that the current bill is worse than no law at all and will harm consumers both in California and nationally.

1. The bill exempts certain direct-to-consumer payday loans from lending laws.

As we previously indicated, it is dangerous to exempt credit products from credit laws. We highlighted the special risks of exempting wage advances when they are provided not through a direct connection to the employer and actual payroll but rather directly to consumers with automatic repayment from the consumer's bank account**. S.B. 472 creates a dangerous precedent by exempting loans from lending laws merely because the consumer "represents" that the advances represent wages that are earned but not yet paid:**

> *"Wage-based advance" or "work-based advance" means funds advanced to a worker by a provider if those funds are based on wages or compensation* ***the worker has represented*** *have been earned but not yet paid to the worker for work performed for or on behalf of an obligor.*

That is exactly what a payday loan is: Funds advanced to a worker ahead of payday. In many if not most cases, consumers who take out payday loans will have earned but unpaid wages. Consumers are unlikely to take out a payday loan immediately on payday. Instead, they seek payday loans after the paycheck has run out but before the next payday. The fact that the worker "represents" to the payday lender that the loans is based on earned but not yet paid wages does not make it any less a loan.

Beyond the payday loans made today by the fintech lenders that claim to be earned wage access providers, **traditional payday lenders could easily devise products that fit into this exemption.** As discussed in greater detail below, even with fees capped, these exempt pay advances could be useful to

payday lenders as starter loans to get people sucked into the cycle of debt – without credit disclosures or protections – that can be exploited to steer the consumer into costly bigger and deeper payday loans.

2. The bill expressly allows payday loans that result in three nonsufficient fund fees, with no limit on overdraft fees.

The bill allows wage advance loans to be repaid automatically from the consumer's bank account—exactly as payday loans are – and anticipates that the repayment of these loans may trigger nonsufficient fund fees – just as payday loans do. This is a far cry from the premise of earned wage access products that enable payment of wages in stages with no loan and no repayment from the consumer that can directly trigger a NSF or overdraft fee.

The amended bill requires only that providers use "best efforts" to ensure sufficient funds when "attempting to collect" from the consumers. **Distressingly, the bill expressly permits repayment practices that could lead to up to three NSF fees.** That is **even higher** than the two NSF fees that payday loans are allowed to trigger under the Consumer Financial Protection Bureau's payday loan rule. **The bill contains no limits whatsoever on the overdraft fees that loan repayment may trigger.** Whether the number of fees is one, two or three, the key point is that these are loans collected from the consumer, not a payment of wages, and the loans can cause trouble if the consumer cannot afford to repay them.

3. The "non-recourse" provisions do not protect consumers from liability.

In an attempt to bolster the claim that direct-to-consumer loans are not in fact loans, the bill now requires that wage advances be provided on a "non-recourse basis"; limits attempts to collect other than direct repayment from the worker "via a means mutually acceptable to the worker and provider"; and provides that a worker shall not be held liable for the employer's failure to meet its payroll obligations. None of these provisions changes the fact that direct-to-consumer advances are loans, nor do these provisions give consumers sufficient protections.

At least one provider currently on the market claims that its loans are "non-recourse" yet includes provisions in its contract that could impose liability on the consumer. The consumer is required to ensure that there are sufficient funds in the account on the repayment day. Thus, the failure of a repayment would be a breach of contract, potentially subjecting the consumer to liability.

Moreover, the bill allows collection attempts by means of any direct repayment means that is "mutually acceptable" – in other words, that is in the fine print of the agreement that a consumer is bound to when clicking "I agree." This gives the lender considerable means to collect the loan.

4. The amended bill increases the permissible cost of pay advances, which could be well in excess of $15/month.

As introduced, the bill capped the cost of pay advances at $14 per month. Even that was too high for the low-wage workers who are likely to use early income access products. That represents nearly two hours of work for a minimum wage worker and undercuts California and federal minimum wage laws. We urged that any exemptions should be limited to products with de minimis fees no more than $5/month in fees (just over $1/week).

Instead, the bill not only raises the monthly amount to $15 but now allows that amount to be based on a six-month average, so that the payments in any given month could be well over $15. While a provider could not “require” payments that exceed $15 in a month, it appears that providers could use purportedly voluntary “tips,” expedite fees, or other methods to extract additional payments. This “tip” model is merely an evasion of credit laws that disguises the cost of credit.

The bill also now explicitly endorses the pernicious practice of charging “expedite” fees for workers who want their wage advance quickly. One provider on the market, for example, charges $1.25 per day extra for each expedited advance of daily pay. Yet virtually any worker who is in need of an advance before payday is going to want that advance quickly. Expedite fees merely hide the cost of the product.

The bill also allows providers to up-sell consumers and charge additional fees for other services. While the provider could not explicitly require the consumer to use these services as a condition of access to wage advances, it could steer consumers into up-sells and add-ons as many companies do. For example, providers that have a connection to payroll could offer overpriced goods and services through a “company store,” allowing for deferred payment through payroll deduction with inflated prices hiding the cost of credit.

5. The bill could allow traditional payday lenders to use 391% APR wage advances as a bait-and-switch opportunity into traditional payday loans.

Under the bill, payday lenders could offer a $100 wage advance loan for $15 – 391% APR, the same price as a traditional payday loan. Two weeks later, the lender could roll the consumer over into another loan at the same price. The lender could charge $30 per month for three months running and then, when the consumer is unable to repay, steer the consumer into a traditional short-term or longer-term payday loan that is not covered by the bill. As long as the payday lender does not make any additional wage advance loans for the next three months, the lender would still meet the six-month $15/month average permitted under the bill.

Or, the payday lender could offer a bigger $300 or $400 payday loan at the $15 price in order to suck the consumer into a bigger debt trap. Indeed, payday lenders have at times offered initial loans for free as a way of luring in consumers. Thus, the price limits in the bill will not deter traditional payday lenders from exploiting the exemptions given.

6. The amended bill worsens the potential for a dangerous cycle of chronic reborrowing.

The original bill capped wage advances at 50% of gross pay. Even that was an inadequate protection. As we described, it is crucial that taxes, wage garnishments, and other deductions be taken into account in order to protect workers from being left with little on the next payday.

Instead of limiting advances to 50% of <u>net</u> pay, as we urged, the amended bill now allows advances to <u>exceed</u> 50% of <u>gross</u> pay twice in a six-month period. This will only exacerbate the potential for consumers to fall into a cycle of needing to re-borrow in order to make up for the shortfall in the paycheck.

The bill also fails to make the other changes we urged to prevent a cycle of chronic overuse. The evidence shows that workers who cannot handle an expense out of the last paycheck frequently cannot handle the hole created in the next paycheck by an earned wage advance, creating a cycle of

dependency virtually identical to the cycle of debt of traditional payday loans. The amended bill fails to adopt our recommendation to:

- Limit early wage access to six instances per year.
- Provide a weaning and cooling off mechanism.
- Strike the provision that prohibits employers from protecting workers with limits stricter than those allowed by the bill.

The failure to address the cycle of debt is especially distressing in light of the failure to exclude direct-to-consumer loans from the bill's provisions.

7. The amended bill now allows providers to require workers to re-direct their entire pay to an account required by the provider.

The original bill prohibited providers from requiring consumers to open up an account at, or to direct deposit earned income to, a particular institution. The amended bill now explicitly allows this practice as long as the worker is not required to pay a fee or charge to open or maintain the account.

Thus, the amended bill now endorses the dangerous practice of at least one earned wage access provider of requiring consumers to re-direct their entire paycheck to an account controlled by the provider, which then syphons off repayment of the wage advance loan and re-distributes the remainder to the consumer's actual account.

The ban on a fee or charge to open or maintain the account is not sufficient to protect the worker. The account could be set up to trigger other types of fees or charges. The provider could also use control over the account to offer expensive loans repaid automatically or otherwise limit the worker's control over their own paycheck. Indeed, the bill does not even require that the account carry deposit insurance.

8. The amended bill eliminates consumer remedies for violations.

The amended bill now makes the $2000 statutory penalty for violations payable only to the Department of Business Oversight, not to the consumer as in the original bill. Thus, providers who violate the bill will have less deterrent and less concern about liability to consumers who are harmed. Consumers also will be deprived of a simple remedy that can cover the wide-ranging costs that violations could impose, including repercussions from the inability to pay rent, food or medical expenses if providers illegally extract funds from the consumer's account.

This is all the more problematic in light of the prevalence of forced arbitration clauses and class action bans in contracts for early wage access products. Thus, consumers must go it alone, before a private arbitrator, who does not even have the power to award a single $2000 penalty.

9. The bill fails to require supervision by the Department of Business Oversight.

The amended bill adds a requirement that providers "register" with the Department of Business Oversight and gives DBO enforcement authority, but the bill does not require licensing or supervision, as we urged. Indeed, the bill explicitly states: "The commissioner shall not be required to conduct routine examinations of a provider." Routine examinations are critical to spot problems that may not otherwise

be apparent. This is especially important with a novel product, particularly one that has such vast potential for abuse. There is no reason that any lender should be exempt from examinations, especially those making direct-to-consumer loans.

10. The modest protections and oversight in the bill do not outweigh the harms, and the bill is especially harmful precedent that will be exploited by payday lenders both in California and nationally.

We appreciate that earned wage access products are already on the market and that they are claiming – rightly or wrongly – that they are not covered by current California (and federal) law. The desire to explicitly bring those products under DBO oversight is understandable. But California may well have tools to regulate these products under current law, and even if it does not, the dangers of the bill outweigh the little gain.

The modest regulation permitted under the bill does not outweigh the harms of blessing a dangerous business model that will impose substantial costs on low-wage workers in California. The cycle of chronic use of earned wage access products is well known. The bill gives California law imprimatur to the evasion of California lending laws for small loans that will do little to help consumers handle unexpected expenses but will simply add fees to their monthly budget and could lead them into incurring hundreds of dollars in direct fees, purportedly voluntary tips and expedite fees, NSF fees and overdraft fees.

The bill creates an especially troubling precedent of accepting the false premise that loans are not loans merely because the consumer "represents" to the lender that they are earned wages. Payday lenders can be expected to exploit this claim both in California – potentially in litigation in ways not currently anticipated – and in other states. This bill, with the modest protections stripped out, will certainly be copied in other states where payday lenders have been eager to get a toehold or are seeking to expand their predatory products.

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Nor these reasons, we must oppose the bill. Thank you for the opportunity to offer our views. If you have any questions, please contact me at (202) 595-7845 or lsaunders@nclc.org.

Yours very truly,

Lauren Saunders
Associate Director
National Consumer Law Center (on behalf of its low income clients)